

Sluggish 1Q19 performance. ERAA recorded a far below estimates 1Q19's readings in which top-line declined by 14% YoY. Bottom-line plunged by 77% YoY as finance costs burdened the profit. Sales was dragged down by cellular phones and tablets segment which was down by 32.3% YoY and the weakening was significantly seen in Central area (Jabodetabek, Kalimantan, Singapore, Malaysia). The company noted a weak iPhone sales for the period, worsened by low demand in Xiaomi and other lower end products, which have been the backbone for ERAA's sales growth in 2018. Competition from black market sellers is also admitted to remain tight which challenges the company's volume and ASP growth. Besides, the deal between Xiaomi and ERAA which should shift responsibility for spare-part imports to Xiaomi have yet to be carried out and gives pressure to ERAA's working capital. Though, ERAA performed a better inventory management as operating CF has turned positive in 1Q19. For 2019, ERAA is targeting 300 additional stores to be opened in 2019 which should serve as a major sales growth driver should being executed successfully (~15% YTD realization).

Smartphone industry gets into a more challenging circumstance.

Indicated through its 1Q19 performance, we think that the industry has gone over its peak in 2017 and started to show declining trend ever since. Global shipments in 2018 dipped by 4.1% YoY, while smartphone leaders have toned down their expectations on future phone sales as households cut spending. The businesses are also increasing focus on IoT and non-hardware services where better opportunities lie.

More low-end units within product mix, leading margin lower.

Recently, flagship handset prices have been surging significantly, though we see feature upgrades are not as compelling as before. As a result, demands for value for money products constantly increase and take larger proportion of product mix which may result in lower blended GPM. This is made clear by the second liner brand spin-off of most Chinese smartphone makers (i.e., Mi and Redmi, Huawei and Honor).

Given the aforementioned conditions, **we lower our recommendation on ERAA to NEUTRAL with a target price of IDR 1,365 which implies FY19F 7.9x P/E as we are cautious on the potential setback on earnings as the industry saturates.** We cut earnings by 40% to reflect softening phone sales demand. Upside risk to our call: IMEI registration implementation, shifting imports for Xiaomi spare, parts and stronger than expected phone sales.

Highlights (IDR bn)	2017	2018	2019F	2020F	2020F
Net Revenue	24,230	34,744	31,035	32,799	34,364
% growth	17.9%	43.4%	-10.7%	5.7%	4.8%
Gross Profit	2,159	3,169	2,754	2,904	3,063
Net Profit	339	850	552	597	620
% growth	28.9%	150.4%	-35.1%	8.1%	4.0%
Gross Margin (%)	8.9%	9.1%	8.9%	8.9%	8.9%
Net Margin (%)	1.4%	2.6%	1.9%	1.9%	1.9%
Return on Equity (%)	9.5%	19.9%	10.9%	10.7%	10.2%
Return on Assets (%)	4.2%	7.9%	4.5%	4.9%	4.9%
EPS	106	266	173	187	194

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Stock Information

Sector	Retail
Bloomberg Ticker	ERAA IJ
Market Cap. (IDR tn)	4.15
Share Out./Float (mn)	3.2/1.4
Current Price	1,450
FY19F Target Price	1,365
Downside	-13.8%

Share Price Performance

52W High (07/30/18)	3,400
52W Low (04/22//19)	1,370
52W Beta	0.4
YTD Change	-40.9%

Relative Valuations

Trailing P/E	5.9
Forward P/E	8.4
P/BV	0.9

Income Statement (IDR Bn)	2017	2018	2019F	2020F	2020F
Revenue	24,230	34,744	31,035	32,799	34,364
Cost of Revenue	22,071	31,575	28,281	29,896	31,302
Gross Profit	2,159	3,169	2,754	2,904	3,063
% growth	20.5%	46.8%	-13.1%	5.4%	5.5%
Operating Expenses	1,636	1,852	1,749	1,914	2,074
Opex to Sales (%)	6.8%	5.3%	5.6%	5.8%	6.0%
EBITDA	673	1,617	1,273	1,273	1,285
% growth	13.4%	140.3%	-21.3%	0.0%	1.0%
EBT	480	1,203	800	860	892
% growth	25.2%	150.8%	-33.5%	7.6%	3.7%
Tax	-133	-314	-209	-224	-233
Non Controlling Interest	8	39	39	39	39
Net Profit for the Year	339	850	552	597	620
% growth	28.9%	150.4%	-35.1%	8.1%	4.0%

Balance Sheet (IDR Bn)	2017	2018	2019F	2020F	2020F
Cash and Cash Equivalent	366	272	446	252	347
Trade Receivables	1,571	1,417	1,266	1,338	1,402
Inventories	3,388	6,795	6,007	6,348	6,674
Other Current Assets	1,359	1,570	1,402	1,482	1,553
Total Current Assets	6,685	10,054	9,121	9,420	9,975
Fixed Assets	486	554	606	582	551
Other Non Current Assets	1,703	2,076	2,242	2,304	2,359
Total Assets	8,874	12,683	11,968	12,306	12,886
Trade Payables	2,619	2,807	2,507	2,650	2,776
ST Bank Loans	1,747	4,284	3,473	3,111	2,990
Other Current Liabilities	682	650	579	612	641
Total Current Liabilities	5,049	7,741	6,559	6,373	6,407
Other Non Current Liabilities	119	117	103	109	114
Total Liabilities	5,167	7,857	6,662	6,481	6,521
Share & APIC	1,884	2,189	2,189	2,189	2,189
Retained Earnings	1,744	2,484	2,965	3,484	4,024
Non Controlling Interest	79	133	133	133	133
Other Components of Equity	(1)	19	19	19	19
Total Equity	3,707	4,826	5,306	5,825	6,365
Total Equity & Liabilities	8,874	12,683	11,968	12,306	12,886

Cash Flow (IDR Bn)	2017	2018	2019F	2020F	2020F
Net Income	339	850	552	597	620
Depreciation	58	70	94	101	110
Chg. in NWC	920	3,386	(642)	272	265
Chg. in Other CT Assets	553	(23)	(107)	51	45
Chg. in Other CT Liabilities	(24)	55	(11)	5	5
CF from Operating	(1,100)	(2,388)	1,383	380	425
Capital Expenditure	87	138	146	78	78
Chg. in LT Assets	(96)	372	166	62	55
Chg in LT Liabilities	37	2	(12)	6	5
CF from Investing	46	(508)	(324)	(135)	(128)
Dividends Paid	(58)	(110)	(72)	(77)	(80)
Chg. in Debt	848	2,533	(814)	(362)	(121)
Share Capital & APIC	-	306	-	-	-
Others	16	73	-	-	-
CF from Financing	806	2,802	(886)	(440)	(202)
Change in Cash	(248)	(94)	174	(194)	95
Beginning Cash	615	366	272	446	252
Ending Cash	366	272	446	252	347

Financial Ratio	2017	2018	2019F	2020F	2020F
Profitability					
ROE	9.5%	19.9%	10.9%	10.7%	10.2%
ROA	4.2%	7.9%	4.5%	4.9%	4.9%
Operating Margin	2.5%	4.4%	3.8%	3.6%	3.5%
Liquidity & Solvency					
Current Ratio	1.3	1.3	1.4	1.5	1.6
Debt to Equity	1.4	1.6	1.3	1.1	1.0
Debt to Assets	0.6	0.6	0.6	0.5	0.5
Interest Coverage	4.2	4.4	2.9	3.4	3.7
Valuation					
Price to Earning (PE)	12.8	5.1	7.9	7.3	7.0
Price to Book (PBV)	0.6	0.9	0.8	0.7	0.7

Key Assumptions	2017	2018F	2019F	2020F	2020F
Number of Stores	775	942	1062	1112	1152
Receivable Days	23	16	16	14	15
Payable Days	39	29	31	29	29
Inventory Days	42	53	75	69	69
Cash Conversion Cycle	25	41	60	55	55

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ADD: Share price may range between 10% to 15% over the next 12 months.

NEUTRAL: Share price may range between -10% to +10% over the next 12 months.

REDUCE: Share price may range between -10% to -15% over the next 12 months.

SELL: Share price may fall by more than 15% over the next 12 months.

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